The Nicest House in the Neighborhood: Finding the Ideal Economic Environment for Your Law Practice

Are you at the "right" law firm? As practices grow, client bases change, and billing rate pressures intensify, your firm's economic environment may no longer be the best fit for you and your practice. In fact, it may be stunting the growth of your practice. Finding the right "neighborhood" for your practice will allow your practice to thrive, thereby maximizing your productivity and your compensation. In order to make the best decision, it is crucial to understand how we got to where we are today.

"It's the Economy, Stupid."

In the simplest terms, the economy has driven firms to where they are today. Firms maximize net income by increasing revenue and keeping overhead low. To increase revenue, a law firm can either raise rates or push their professionals to work harder, or both. All that changed in 2008.

Take one well-known litigation firm as an example. During the high-flying, cash rich days, most of their associates were made "Partners" after only eight or nine years. They could be billed at higher rates, and clients allowed litigation matters to be heavily staffed.

CAUSE	EFFECT
Pre-2008 and the Thriving Economy	When the economy was thriving, law firms could increase rates for their services and had higher overhead with larger profit margins. Firms were flush with cash, litigation was active, and clients were willing to pay.
2008 Economic Recession and Thereafter	As the Recession took hold, clients that were quick to litigate, were now quick to settle. Firms were forced to reduce support staff, eliminate underutilized attorneys, and cut rates. Law firm profit margins were pinched.

After the Recession, clients preferred the certainty of settling and litigation dried up. The firm had high overhead, was paying too many "Partners", did not adjust quickly enough, and the firm went under.

Other firms were forced to adjust or suffer the consequences. With the economy in the dumps, clients cracked down on billing rates, and asked for discounts and reduced rates to stick with their preferred law firms. Clients created preferred provider lists, forcing law firms to start operating more like a business. That has continued to this day. Clients monitor staffing levels, are unwilling to pay for associates to learn on the job, and closely monitor billing rates.

The Haves and the Have Nots

Clients are still willing to pay premium rates ($900 an hour and up) for premium work — paying top dollar for the best talent and heavily staffing matters for "bet the company" litigation or a major transaction. The top firms doing premium work (mostly based in New York) have become significantly more profitable in recent years, while other firms have been

Partners need to look at their practice and decide if they need to move to a nicer or a more modest neighborhood. The question is not "Which is the Best Neighborhood?", but "Which is the Best Neighborhood for me and my practice?

forced to cut overhead, closely monitor rates, and make hard decisions on underperforming associates and partners. Most law firms have cut overhead as much as they can (or are willing to), and cannot increase staffing levels significantly. So, to increase profitability, law firms have tried to gently raise rates. Sometimes that works. Sometimes, it doesn't. The question to ask yourself: "Where does this leave my practice, and how does my practice compare to my Partners' practices?"

The Neighborhood Rule

Let me introduce you to the neighborhood rule. How does your practice compare to those around you? If you have the nicest house (practice) in the neighborhood (your firm), you are adding more value to your neighbors' houses than they are adding to yours. In fact, the neighborhood is bringing down the value of your house. So, if your practice is the largest in the firm or you are billing at a higher rate than everyone around you, it is time to move to a better neighborhood. You will benefit from the higher profit margins of the higher billing practices around you, and (likely) be at a more profitable law firm, getting paid more for the same amount of work. Your clients are also more likely to look like your (new) partners' clients.

On the other hand, if everyone around you has a nicer house than yours, and you are being pushed to make changes you cannot "afford", that is not good either. In other words, if your law firm is pushing you to raise rates, which could potentially alienate your clients, you need to look at your options. Lowering your rates may actually help your practice grow, allowing you to do more for your current clients, while attracting new ones. Either way, you will end up billing more, and doing better than you would have, had you stayed at the more profitable firm and been forced to (uncomfortably) increase your rates.

In What Neighborhood Will Your Practice Thrive?

Partners need to look at their practice and decide if they need to move to a nicer or a more modest neighborhood. The question is not, "Which is the Best Neighborhood?", but "Which is the Best Neighborhood for me and my practice?"

Can I make more money by moving to a firm in which other practices are as profitable as mine? A firm where my practice is not "the nicest house on the block", but now looks like my neighbors' houses, will help my practice (and my compensation) grow. Perhaps I should be considering a more profitable firm, or a full-service firm (if currently at a specialty firm).

It is always tempting to live in the nicer neighborhood. However, if your practice will thrive at a slightly less profitable firm, with less billing rate pressure, perhaps moving to a more modest neighborhood will benefit your practice. It is one step back, but two steps forward for you and your practice. Your practice will grow, and you will be more highly rewarded.

Our 30 years of experience in the legal industry have taught us that it is crucial that you find the right "neighborhood." Once you are in the law firm best suited to you and your practice, you will then be able to flourish, grow, and thrive! ■

Mestel from the Bench | Meet our Thought Leader

Howard Parris, Esq.
EXECUTIVE MANAGING DIRECTOR.
PARTNERS, GROUPS, AND MERGERS.
WASHINGTON, DC
hparris@mestel.com

"Getting to know a candidate and their practice, building a relationship, staying in touch, and when necessary, finding the right firm, is what I do."